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Office of the Legislative Auditor

State of Montana



Report to the Legislature

September 1989

Financial Audit

Fiscal Year Ended June 30, 1989

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Guaranteed Student Loan Program

Commissioner of Higher Education

We issued an unqualified opinion on the financial statements of the program and our report contains no recommendations.

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Direct comments/inquiries to:
Office of the Legislative Auditor
Room 135, State Capitol
Helena, Montana 59620



FINANCIAL-COMPLIANCE AUDITS

Financial-compliance audits are conducted by the Office of the Legislative Auditor to determine if an agency's financial operations are properly conducted, the financial reports are presented fairly, and the agency has complied with applicable laws and regulations which could have a significant financial impact. In performing the audit work, the audit staff uses standards set forth by the American Institute of Certified Public Accountants and the United States General Accounting Office. Financial-compliance audit staff members hold degrees with an emphasis in accounting. Most staff members hold Certified Public Accountant (CPA) certificates.

The Single Audit Act of 1984 and OMB Circular A-128 require the auditor to issue certain financial, internal control, and compliance reports regarding the state's federal financial assistance programs, including all findings of noncompliance and questioned costs. This individual agency audit report is not intended to comply with the Single Audit Act of 1984 or OMB Circular A-128 and is therefore not intended for distribution to federal grantor agencies. The Office of the Legislative Auditor issues a statewide biennial Single Audit Report which complies with the reporting requirements listed above. The Single Audit Report for the two fiscal years ended June 30, 1987 has been issued. Copies of the Single Audit Report can be obtained by contacting:

Office of the Legislative Auditor
Room 135, State Capitol
Helena, MT 59620

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Representative Bruce Simon



STATE OF MONTANA
Office of the Legislative Auditor

STATE CAPITOL
HELENA, MONTANA 59620
406/444-3122

LEGISLATIVE AUDITOR:
SCOTT A. SEACAT

LEGAL COUNSEL:
JOHN W. NORTHEY

September 1989

DEPUTY LEGISLATIVE AUDITORS:

MARY BRYSON
Operations and EDP Audit

JAMES GILLET
Financial-Compliance Audit

JIM PELLEGRINI
Performance Audit

The Legislative Audit Committee
of the Montana State Legislature:

This is our report on the audit of the Commissioner of Higher Education's Guaranteed Student Loan Program (GSL) for the fiscal year ended June 30, 1989.

The Montana Guaranteed Student Loan Program, established by the 46th Montana Legislature, allows eligible students to receive guaranteed loans from lender institutions. The federal government guarantees the loans made by lending institutions. The federal government also advances start-up money and makes administrative cost reimbursements to GSL.

The Guaranteed Student Loan program initially contracted with United Student Aid Funds to service loans. In the fall of 1987 the Board of Regents approved a plan to bring the loan servicing to Montana. The Guaranteed Student Loan program began the phase-in process in April 1988 and expects the process to be complete by March 1990.

We thank the Commissioner of Higher Education and his staff for their cooperation and assistance during the audit.

Respectfully submitted,

A handwritten signature in black ink, appearing to read "Scott A. Seacat", with a long, sweeping horizontal line extending to the right.

Scott A. Seacat
Legislative Auditor

**Guaranteed Student Loan Program
Commissioner of Higher Education**

**Financial Audit for the
Fiscal Year Ended June 30, 1989**



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INDEPENDENT AUDITOR'S REPORT AND
AGENCY FINANCIAL STATEMENTS



Office of the Legislative Auditor

STATE CAPITOL
HELENA, MONTANA 59620
406/444-3122

LEGISLATIVE AUDITOR:
SCOTT A. SEACAT

LEGAL COUNSEL:
JOHN W. NORTHEY

DEPUTY LEGISLATIVE AUDITORS:

MARY BRYSON
Operations and EDP Audit

JAMES GILLETT
Financial-Compliance Audit

JIM PELLEGRINI
Performance Audit

INDEPENDENT AUDITOR'S REPORT

The Legislative Audit Committee
of the Montana State Legislature:

We have audited the Balance Sheet of the Guaranteed Student Loan Program - Special Revenue Fund of the state of Montana as of June 30, 1989, and the related Statement of Revenues, Expenditures and Changes in Fund Balance - Budget and Actual for the fiscal year then ended. These financial statements are the responsibility of the Program's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Guaranteed Student Loan Program of the state of Montana as of June 30, 1989, and the results of its operations for the year then ended in conformity with generally accepted accounting principles.

Respectfully submitted,

A handwritten signature in cursive script that reads "James Gillett".

James Gillett, CPA
Deputy Legislative Auditor

August 29, 1989

COMMISSIONER OF HIGHER EDUCATION
GUARANTEED STUDENT LOAN PROGRAM
SPECIAL REVENUE FUND
BALANCE SHEET
JUNE 30, 1989

ASSETS

Cash in Treasury	\$ 76,227
Interest Receivable	509
Accounts Receivable	12,195
Prepaid Expenses	3,919
Due From Federal Government (Notes 4, 7)	2,044,321
Investments (Note 3)	<u>2,547,300</u>
TOTAL ASSETS	<u>\$4,684,471</u>

LIABILITIES AND FUND BALANCES

Liabilities:

Accounts Payable	\$ 2,000
Due to Federal Government (Note 8)	224,625
Deferred Revenue	<u>2,939,334</u>
TOTAL LIABILITIES	3,165,959

Fund Balances:

Restricted (Note 5)	89,112
Unrestricted	<u>1,429,400</u>
TOTAL FUND BALANCE (Note 7)	1,518,512

TOTAL LIABILITIES AND FUND BALANCES	<u>\$4,684,471</u>
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The accompanying notes are an integral part of this financial statement.

COMMISSIONER OF HIGHER EDUCATION
 GUARANTEED STUDENT LOAN PROGRAM
 SPECIAL REVENUE FUND
 STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCE
 BUDGET AND ACTUAL
 FOR THE YEAR ENDING JUNE 30, 1989

	<u>Budget</u>	<u>Actual</u>	Variance Favorable <u>(Unfavorable)</u>
REVENUE:			
Guarantee Fee Income	\$ 600,000	\$ 704,460	\$ 104,460
Administrative Cost			
Allow. (Note 6)	359,000	428,699	69,699
Investment Income	300,000	225,317	(74,683)
Collection Cost Retained	50,000	28,828	(21,172)
Recoveries of Defaults	<u>25,000</u>	<u>22,753</u>	<u>(2,247)</u>
TOTAL REVENUES	1,334,000	1,410,057	76,057
 EXPENDITURES:			
Administrative Costs	1,361,493	1,132,788	228,705
Equipment and Intangible Assets	<u>55,000</u>	<u>71,149</u>	<u>(16,149)</u>
TOTAL EXPENDITURES	1,416,493	1,203,937	212,556
 Excess Revenues Over/ (Under) Expenditures	(82,493)	206,120	288,613
 Prior Year Adjustment (Note 9)	0	(14,723)	(14,723)
 Fund Balance - 07/01/88	<u>1,327,115</u>	<u>1,327,115</u>	<u>0</u>
 Fund Balance - 06/30/89 (Note 7)	<u>\$1,244,622</u>	<u>\$1,518,512</u>	<u>\$ 273,890</u>

The accompanying notes are an integral part of this financial statement.

COMMISSIONER OF HIGHER EDUCATION
GUARANTEED STUDENT LOAN PROGRAM
NOTES TO THE FINANCIAL STATEMENTS
FOR THE YEAR ENDING JUNE 30, 1989

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. Description of Program

The state of Montana Guaranteed Student Loan (GSL) Program is located in the Office of the Commissioner of Higher Education. As an Other Special Revenue Fund, it accounts for the proceeds of revenue sources that are legally restricted to expenditures for specified purposes. The program was established by the Office of the Commissioner of Higher Education in fiscal year 1981 to coordinate and administer the federally insured student loans issued by various lending institutions within the state of Montana.

B. Basis of Accounting

The financial statements were prepared using the modified accrual basis of accounting. Under the modified accrual basis of accounting, expenditures are recorded on the basis of valid obligations. Revenues are recorded when received in cash unless susceptible to accrual.

Revenues are susceptible to accrual if they are measurable and available to finance expenditures of the fiscal period or are not received at the normal time of receipt. Revenues are deferred if material and are received before the normal time of receipt or if received for a particular activity and the expense for that activity has not been incurred prior to fiscal year end.

2. EMPLOYEES' RETIREMENT SYSTEM

The Guaranteed Student Loan Program employees are covered by either the Public Employees' Retirement System (PERS) or the Teachers' Retirement System (TRS), or the University System Optional Retirement Plan, TIAA-CREF.

Under PERS, the state contributes 6.417% of an employee's gross wages to PERS. The employee contributes 6.0% of his gross wages. Through the fiscal year ending June 30, 1989, GSL contributed \$7,603 to PERS in employer contributions.

Under TRS, the state contributes 7.428% of an employee's gross wages to TRS. The employee contributes 7.044% of his gross wages. Through the fiscal year ending June 30, 1989, GSL contributed \$7,049 to TRS in employer contributions.

Under TIAA-CREF, the state contributes 2.956% to TIAA and 4.472% to TRS. The employee contributes 7.044% of his gross wages to TIAA. Through the fiscal year ending June 30, 1989, GSL contributed \$338 to TIAA.

The State's policy is to fund accrued pension costs although unfunded liabilities exist. Based on their most recent actuarial valuation reports, both the PERS and the TRS were actuarially sound.

3. INVESTMENTS

Investments are units purchased in the state of Montana's Short Term Investment Pool and are reflected at cost. The June 30, 1989, balance reflects the following:

<u>Number of Units</u>	<u>Cost</u>
25,473	\$2,547,300

4. DUE FROM FEDERAL GOVERNMENT

United Student Aid Funds (USAF) pays individual lending institutions for any loans that have been defaulted or are unpaid due to the death of the borrower. The GSL program reimburses USAF for the amounts paid on death and default claims. The GSL program then seeks reimbursement from the Department of Education for payments made to USAF for the death and default claims. The extent of this outstanding activity is shown below:

Claims due from D.E.	\$1,014,282
Plus ACA 4th quarter (Note 6)	61,981
Total spenddown receivable (Note 7)	<u>968,058</u>
	<u>\$2,044,321</u>

5. RESTRICTED INCOME FUND BALANCE

This fund balance accounts for all interest earnings on the advance discussed in Note 7 as program regulations require these interest earnings be maintained for claim payments. Through 06/30/89 GSL has paid \$183,051 in claims.

6. ADMINISTRATIVE COST ALLOWANCE

The Administrative Cost Allowance (ACA) revenue is \$428,699 for the fiscal year ending June 30, 1989. This allowance is dependent upon the federal appropriation. It represents 1% of the loans guaranteed for the quarter. The Dept. of Education has credited GSL's first quarter ACA as part of its spenddown plan.

7. LITIGATION

The program received \$734,173 during the first six years of its operation from the United States Department of Education to assist the program in its start-up stages. These funds were restricted in their use and could be recalled by the federal government if the reserve maintained by the program exceeded certain requirements. At the end of February, 1988, GSL returned \$493,830 of the original advance to the U.S. Department of Education and the final \$240,343 was returned during November 1988. The Department of Education also notified GSL that the program must reduce its reserves by an additional \$968,058. GSL joined four other states in filing suit in federal district court in Denver to have this action declared unconstitutional.

This suit is one of almost a dozen such suits going on in various federal courts around the country. So far decisions have been rendered in six of those cases. In three of them the student loan agencies have prevailed and in three other cases the federal government has prevailed. Some, or all, of these decisions have been appealed to the circuit court level but no decisions have yet been rendered there.

The Department of Education withheld payments September, 1988 through November, 1988 in order to satisfy their spenddown requirement of \$968,058 from Montana's Guaranteed Student Loan Program. Should the Department of Education prevail, the balances of GSL as of the June 30, 1989 balance sheet date would be adversely affected as follows:

	Current Balance	Balance if D.E. prevails
Due from Federal Gov't	\$2,044,321	\$1,076,263
Total Assets	\$4,684,471	\$3,716,413
Fund Balance:		
Restricted	\$89,112	\$89,112
Unrestricted	\$1,429,400	\$461,342
Total Fund Balance	\$1,518,512	\$550,454
Total Liabilities & Fund Balances	\$4,684,471	\$3,716,413

8. DUE TO FEDERAL GOVERNMENT

USAF seeks collection of loans that have been defaulted. Upon collection of all or a portion of a defaulted loan, USAF deducts an amount, not to exceed 30% of the collected amount, as a collection fee, and gives the balance to the GSL program. Since the GSL program previously received payment for the defaulted loan from the Department of Education, the amount of the new loan recovery is owed back to the Department of Education. The extent of this outstanding activity is shown below:

Claims due to D.E.	<u>\$224,625</u>
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9. PRIOR YEAR ADJUSTMENTS

The prior year adjustment of (\$14,723) includes \$9,656 which was the amount by which the reinsurance fee accrual was overstated at fiscal year-end (FYE) 1988 and (\$24,722) which was an overestimation of the administrative cost allowance revenue accrual for FY 88 due to accruing revenue on consolidated loans. The remainder of the prior year adjustment was caused by paying bills during FY 89 which were incurred during FY 88.

AGENCY RESPONSE



THE MONTANA UNIVERSITY SYSTEM

35 SOUTH LAST CHANCE GULCH
HELENA, MONTANA 59620-3104
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COMMISSIONER OF HIGHER EDUCATION

MONTANA GUARANTEED STUDENT LOAN PROGRAM

September 18, 1989

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Montana Legislative Auditor

Scott Seacat
Legislative Auditor
Capitol Station
Helena, MT 59620

Dear Scott:

This letter confirms completion of the audit your staff performed on the Guaranteed Student Loan Program. It is my understanding that there are no recommendations.

I want to take this opportunity to thank you and your staff for the fine spirit of cooperation. I also find it gratifying that two members of your staff have audited this program for a number of years. This continuity has helped the staff evaluate the program and implement procedures that are in the best interest of the student borrowers, the lenders and the school. I want to especially thank Lorri Parriman and Susan Fleming for their cooperation.

Sincerely,

A handwritten signature in cursive script, reading "Bill Lannan".

Bill Lannan, Director
Guaranteed Student Loan Program

